

# Report of the auditor-general to the Free State Legislature and the council on the Mantsopa Local Municipality

## Report on the audit of the financial statements

### Qualified opinion

1. I have audited the financial statements of the Mantsopa Local Municipality set out on pages ... to ..., which comprise the statement of financial position as at 30 June 2018, the statement of financial performance, statement of changes in net assets, cash flow statement and statement of comparison of budget and actual amounts for the year then ended, as well as the notes to the financial statements, including a summary of significant accounting policies.
2. In my opinion, except for the possible effects of the matters described in the basis for qualified opinion section of this auditor's report, the financial statements present fairly, in all material respects, the financial position of the Mantsopa Local Municipality as at 30 June 2018, and its financial performance and cash flows for the year then ended in accordance with the South African Standards of Generally Recognised Accounting Practice (SA Standards of GRAP) and the requirements of the Municipal Finance Management Act of South Africa, 2003 (Act No. 56 of 2003) (MFMA) and the Division of Revenue Act of South Africa, 2017 (Act No. 3 of 2017) (Dora).

### Basis for qualified opinion

#### Service charges

3. The municipality did not recognise service charges in accordance with GRAP 9, *Revenue from exchange transactions*. Service charges were incorrectly calculated and levied on consumer accounts. Consequently, I was unable to determine the full extent of the understatement on service charges and receivables from exchange transactions, as it was impracticable to do so. Additionally, there was a resultant impact on the deficit for the year and on the accumulated surplus.

### Context for the opinion

4. I conducted my audit in accordance with the International Standards on Auditing (ISAs). My responsibilities under those standards are further described in the auditor-general's responsibilities for the audit of the financial statements section of this auditor's report.
5. I am independent of the municipality in accordance with the International Ethics Standards Board for Accountants' *Code of ethics for professional accountants* (IESBA code) and the ethical requirements that are relevant to my audit in South Africa. I have fulfilled my other ethical responsibilities in accordance with these requirements and the IESBA code.
6. I believe that the audit evidence I have obtained is sufficient and appropriate to provide a basis for my qualified opinion.

## **Material uncertainty relating to going concern**

7. I draw attention to the matter below. My opinion is not modified in respect of this matter.
8. Note 45 to the financial statements indicates that the municipality incurred a net loss of R107 376 653 during the year ended 30 June 2018 and, as of that date, the municipality's current liabilities exceeded its current assets by R132 657 475. The municipality has been deducting pension, medical aid and pay as you earn from employees' salaries, but has been unable to pay over R10 270 321 (2017: R4 239 781) of these amounts to the relevant third parties. In addition, the municipality owed Eskom R135 354 844 (2017: R129 699 446) as at 30 June 2018, which is long overdue. These events or conditions, along with other matters as set forth in note 45, indicate that a material uncertainty exists that may cast significant doubt on the municipality's ability to continue as a going concern.

## **Emphasis of matters**

9. I draw attention to the matters below. My opinion is not modified in respect of these matters.

### **Unauthorised expenditure**

10. As disclosed in note 46 to the financial statements, the municipality incurred unauthorised expenditure of R169 756 083 (2017: R96 701 149) in the year under review, due to the overspending of the approved budget.

### **Irregular expenditure**

11. As disclosed in note 48 to the financial statements, the municipality incurred irregular expenditure of R1 894 934 (2017: R7 344 653), and R9 191 671 was identified in the current year in respect of prior years. The irregular expenditure was mainly due to non-compliance with Supply Chain Management (SCM) Regulations.

### **Fruitless and wasteful expenditure**

12. As disclosed in note 47 to the financial statements, the municipality incurred fruitless and wasteful expenditure of R15 616 019 (2017: R14 234 005) during the year, due to interest and penalty charges on the late payment of suppliers.

### **Restatement of corresponding figures**

13. As disclosed in note 42 to the financial statements, the corresponding figures for 30 June 2017 were restated as a result of an error in the financial statements of the municipality at, and for the year ended, 30 June 2018.

### **Material losses**

14. As disclosed in note 52 to the financial statements, water distribution losses of R1 969 373 (2017: R1 724 285) and electricity distribution losses of R13 348 706 (2017: R13 973 066) were incurred, which represented 49% (2017: 42%) and 32% (2017: 32%) of the total water and electricity purchased, respectively. These losses by the municipality were due to illegal connections, leakages, burst water pipes, line losses, tampering and theft.

### **Material impairment**

15. As disclosed in note 7 to the financial statements, receivables from exchange and non-exchange transactions were impaired by R289 435 060 (2017: R167 607 378).

### **Other matters**

16. I draw attention to the matters below. My opinion is not modified in respect of these matters.

### **Unaudited disclosure notes**

17. In terms of section 125(2)(e) of the MFMA, the municipality is required to disclose particulars of non-compliance with the MFMA in the financial statements. This disclosure requirement did not form part of the audit of the financial statements and, accordingly, I do not express an opinion thereon.

### **Unaudited supplementary information**

18. The supplementary information set out on pages xx to xx does not form part of the financial statements and is presented as additional information. I have not audited these schedules and, accordingly, I do not express an opinion on them.

### **Responsibilities of the accounting officer for the financial statements**

19. The accounting officer is responsible for the preparation and fair presentation of the financial statements in accordance with the SA Standards of GRAP and the requirements of the MFMA and Dora, and for such internal control as the accounting officer determines is necessary to enable the preparation of financial statements that are free from material misstatement, whether due to fraud or error.
20. In preparing the financial statements, the accounting officer is responsible for assessing the Mantsopa Local Municipality's ability to continue as a going concern, disclosing, as applicable, matters relating to going concern and using the going concern basis of accounting unless the appropriate governance structure either intends to liquidate the municipality or to cease operations, or has no realistic alternative but to do so.

### **Auditor-general's responsibilities for the audit of the financial statements**

21. My objectives are to obtain reasonable assurance about whether the financial statements as a whole are free from material misstatement, whether due to fraud or error, and to issue an auditor's report that includes my opinion. Reasonable assurance is a high level of assurance, but is not a guarantee that an audit conducted in accordance with the ISAs will always detect a material misstatement when it exists. Misstatements can arise from fraud or error and are considered material if, individually or in aggregate, they could reasonably be expected to influence the economic decisions of users taken on the basis of these financial statements.
22. A further description of my responsibilities for the audit of the financial statements is included in the annexure to this auditor's report.

## Report on the audit of the annual performance report

### Introduction and scope

23. In accordance with the Public Audit Act of South Africa, 2004 (Act No. 25 of 2004) (PAA) and the general notice issued in terms thereof, I have a responsibility to report material findings on the reported performance information against predetermined objectives for selected key performance areas (KPAs) presented in the annual performance report. I performed procedures to identify findings but not to gather evidence to express assurance.
24. My procedures address the reported performance information, which must be based on the approved performance planning documents of the municipality. I have not evaluated the completeness and appropriateness of the performance indicators/measures included in the planning documents. My procedures also did not extend to any disclosures or assertions relating to planned performance strategies and information in respect of future periods that may be included as part of the reported performance information. Accordingly, my findings do not extend to these matters.
25. I evaluated the usefulness and reliability of the reported performance information in accordance with the criteria developed from the performance management and reporting framework, as defined in the general notice, for the following selected KPA presented in the annual performance report of the municipality for the year ended 30 June 2018:

KPA	Pages in the annual performance report
KPA 1 – basic service and infrastructure development	x – x

26. I performed procedures to determine whether the reported performance information was properly presented and whether performance was consistent with the approved performance planning documents. I performed further procedures to determine whether the indicators and related targets were measurable and relevant, and assessed the reliability of the reported performance information to determine whether it was valid, accurate and complete.
27. The material findings in respect of the usefulness and reliability of the selected KPA are as follows:

#### KPA 1 – basic service and infrastructure development

##### Monthly clearing of 35 illegal dumping sites

28. The planned target for this indicator was not specific in clearly identifying the nature and required level of performance, and was also not measurable.

### Various indicators

29. The reported achievements in the annual performance report did not agree to the supporting evidence provided for the indicators listed below. The supporting evidence provided indicated that the achievements of these indicators were as follows:

Indicator description	Reported achievement	Audited value
Number of storm water channels maintained	4	8
Square metres of potholes repaired	18 703	0
Kilometres of roads gravelled	8 094	0
Monthly clearing of 35 illegal dumping sites	760	1 295

### Other matters

30. I draw attention to the matters below.

### Achievement of planned targets

31. Refer to the annual performance report on pages xx to xx for information on the achievement of planned targets for the year. This information should be considered in the context of the material findings on the usefulness and reliability of the reported performance information in paragraphs 28 to 29 of this report.

### Adjustment of material misstatements

32. I identified material misstatements in the annual performance report submitted for auditing. These material misstatements were on the reported performance information of KPA 1 – basic service and infrastructure development. As management subsequently corrected only some of the misstatements, I raised material findings on the usefulness and reliability of the reported performance information. Those that were not corrected are reported above.

## Report on the audit of compliance with legislation

### Introduction and scope

33. In accordance with the PAA and the general notice issued in terms thereof, I have a responsibility to report material findings on the compliance of the municipality with specific matters in key legislation. I performed procedures to identify findings but not to gather evidence to express assurance.
34. The material findings on compliance with specific matters in key legislation are as follows:



### **Annual financial statements**

35. The financial statements submitted for auditing were not prepared in all material respects in accordance with the requirements of section 122(1) of the MFMA. Material misstatements of current assets, current liabilities, revenue, expenditure and disclosure items identified by the auditors in the submitted financial statements were subsequently corrected and the supporting records were subsequently provided, but the uncorrected material misstatements and supporting records that could not be provided resulted in the financial statements receiving a qualified audit opinion.

### **Expenditure management**

36. Money owed by the municipality was not always paid within 30 days, as required by section 65(2)(e) of the MFMA.
37. Reasonable steps were not taken to prevent irregular expenditure, as required by section 62(1)(d) of the MFMA.
38. Effective steps were not taken to prevent fruitless and wasteful expenditure amounting to R15 565 864, as disclosed in note 46 to the annual financial statements, in contravention of section 62(1)(d) of the MFMA. The majority of the disclosed fruitless and wasteful expenditure was caused by interest on overdue accounts of suppliers.
39. Reasonable steps were not taken to prevent unauthorised expenditure amounting to R169 756 083, as disclosed in note 45 to the annual financial statements, in contravention of section 62(1)(d) of the MFMA.

### **Revenue management**

40. An effective system of internal control for debtors and revenue was not in place, as required by section 64(2)(f) of the MFMA.

### **Asset management**

41. An adequate management, accounting and information system was not in place to account for assets, as required by section 63(2)(a) of the MFMA.

### **Consequence management**

42. Unauthorised expenditure incurred by the municipality was not investigated to determine if any person is liable for the expenditure, as required by section 32(2)(a) of the MFMA.
43. The authorisation of unauthorised expenditure amounting to R169 753 083 was not done through an adjustment budget, as required by section 32(2)(a)(i) of the MFMA.
44. Irregular expenditure incurred by the municipality was not investigated to determine if any person is liable for the expenditure, as required by section 32(2)(b) of the MFMA.
45. Fruitless and wasteful expenditure incurred by the municipality was not investigated to determine if any person is liable for the expenditure, as required by section 32(2)(b) of the MFMA.

## Procurement and contract management

46. Goods and services with a transaction value below R200 000 were procured without obtaining the required price quotations, in contravention of SCM regulation 17(a) and (c). Similar non-compliance was also reported in the prior year.
47. The performance of some of the contractors or providers was not monitored on a monthly basis, as required by section 116(2)(b) of the MFMA.
48. The contract performance and monitoring measures and methods were not sufficient to ensure effective contract management, as required by section 116(2)(c) of the MFMA. Similar non-compliance was also reported in the prior year.
49. Awards were made to providers who were in the service of other state institutions or whose directors were in the service of other state institutions, in contravention of section 112(j) of the MFMA and SCM regulation 44. Similar awards were identified in the previous year and no effective steps were taken to prevent or combat the abuse of the SCM process, as required by SCM regulation 38(1).
50. Persons in the service of the municipality whose close family members had a private or business interest in contracts awarded by the municipality failed to disclose such interest, in contravention of SCM regulation 46(2)(e) issued in terms of the Municipal Systems Act of South Africa, 2000 (Act No. 32 of 2000).

## Other information

51. The accounting officer is responsible for the other information. The other information comprises the information included in the annual report. The other information does not include the financial statements, the auditor's report and the selected KPA presented in the annual performance report that has been specifically reported in this auditor's report.
52. My opinion on the financial statements and findings on the reported performance information and compliance with legislation do not cover the other information and I do not express an audit opinion or any form of assurance conclusion thereon.
53. In connection with my audit, my responsibility is to read the other information and, in doing so, consider whether the other information is materially inconsistent with the financial statements and the selected KPAs presented in the annual performance report, or my knowledge obtained in the audit, or otherwise appears to be materially misstated.
54. I did not receive the other information prior to the date of this auditor's report. When I do receive and read this information, and if I conclude that there is a material misstatement therein, I am required to communicate the matter to those charged with governance and request that the other information be corrected. If the other information is not corrected, I may have to retract this auditor's report and re-issue an amended report as appropriate. However, if it is corrected this will not be necessary.

## Internal control deficiencies

55. I considered internal control relevant to my audit of the financial statements, reported performance information and compliance with applicable legislation; however, my objective was not to express any form of assurance on it. The matters reported below are limited to the significant internal control deficiencies that resulted in the basis for the qualified opinion, the findings on the annual performance report and the findings on compliance with legislation included in this report.
56. Leadership did not provide sufficient oversight of financial and performance reporting and compliance as well as related internal controls, as repeat material findings were identified in the current year.
57. Leadership did not implement adequate and effective monitoring controls over the implementation of actions to address prior year reported matters. This resulted in repeat findings that had not been addressed.
58. Leadership did not take effective steps to ensure that there were consequences for poor performance and transgressions, as no official was held responsible for the unauthorised, irregular, and fruitless and wasteful expenditure incurred by the municipality.
59. Management did not prioritise the review and monitoring of compliance with legislation, which resulted in repeat findings being reported. This was due to a lack of consequence management, as officials were not held accountable for non-compliance.
60. Management did not implement adequate review and supervisory controls over financial and performance reporting so that errors could be timeously identified and corrected, resulting in significant repeat findings that could have been prevented.
61. Management did not adequately implement risk management strategies to prevent or mitigate risks relating to financial and performance reporting, as risks to financial and performance reporting were not timeously detected or prevented. This was mainly due to the inadequate implementation of risk strategies by management.

*Auditor - General*

Bloemfontein

30 November 2018



AUDITOR - GENERAL  
SOUTH AFRICA

*Auditing to build public confidence*



## **Annexure – Auditor-general’s responsibility for the audit**

1. As part of an audit in accordance with the ISAs, I exercise professional judgement and maintain professional scepticism throughout my audit of the financial statements, and the procedures performed on reported performance information for selected KPAs and on the municipality’s compliance with respect to the selected subject matters.

### **Financial statements**

2. In addition to my responsibility for the audit of the financial statements as described in this auditor’s report, I also:
  - identify and assess the risks of material misstatement of the financial statements whether due to fraud or error, design and perform audit procedures responsive to those risks, and obtain audit evidence that is sufficient and appropriate to provide a basis for my opinion. The risk of not detecting a material misstatement resulting from fraud is higher than for one resulting from error, as fraud may involve collusion, forgery, intentional omissions, misrepresentations, or the override of internal control
  - obtain an understanding of internal control relevant to the audit in order to design audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the municipality’s internal control
  - evaluate the appropriateness of accounting policies used and the reasonableness of accounting estimates and related disclosures made by the accounting officer
  - conclude on the appropriateness of the accounting officer’s use of the going concern basis of accounting in the preparation of the financial statements. I also conclude, based on the audit evidence obtained, whether a material uncertainty exists related to events or conditions that may cast significant doubt on the Mantsopa Local Municipality’s ability to continue as a going concern. If I conclude that a material uncertainty exists, I am required to draw attention in my auditor’s report to the related disclosures in the financial statements about the material uncertainty or, if such disclosures are inadequate, to modify the opinion on the financial statements. My conclusions are based on the information available to me at the date of this auditor’s report. However, future events or conditions may cause a municipality to cease continuing as a going concern
  - evaluate the overall presentation, structure and content of the financial statements, including the disclosures, and whether the financial statements represent the underlying transactions and events in a manner that achieves fair presentation

### **Communication with those charged with governance**

3. I communicate with the accounting officer regarding, among other matters, the planned scope and timing of the audit and significant audit findings, including any significant deficiencies in internal control that I identify during my audit.
4. I also confirm to the accounting officer that I have complied with relevant ethical requirements regarding independence, and communicate all relationships and other matters that may reasonably be thought to have a bearing on my independence and, where applicable, related safeguards.